IB 96-261

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February 6, 1997

William F. Caton
Acting Secretary
Office of the Secretary
Federal Communications Commission
1919 M Street N.W.
Washington, D.C. 20554

Dear Mr. Caton:

I refer to the Federal Communications Commission's Notice of Proposed Rulemaking adopted on December 19, 1996. Please find attached the Japanese Comments on the International Settlement Rate benchmark proposed by FCC. I would be very grateful if you take our comments fully into consideration.

Sincerely,

Junichiro Miyazaki

Junichiro Miyazaki
Counselor of Embassy of Japan

Attachments:

Comments on the International Settlement Rate benchmark proposed by FCC

cc: Mr. William Corbett

Mr. Richard Beaird

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Comments on the International Settlement Rate benchmark proposed by the Federal Communications Commission (FCC)

The Government of Japan (GOJ) hereby submits the following comments in response to the Commission's Notice of Proposed Rulemaking ("NPRM"(IB Docket No. 96 - 261)). The comments are not exhaustive and the GOJ may submit additional points in the future, as appropriate.

1. The GOJ shares the view with the Government of the United States (USG) that international settlement rates should be reduced and cost-based, and it has actively participated in discussion on the international settlement rate system in various international fora including the International Telecommunication Union (ITU). However, the NPRM proposed by the FCC gives rise to numerous problems that need to be addressed.

2. International settlement rates should be decided based on commercial contracts between carriers. Even if a government is involved in setting targets for international settlement rates, consideration must be made on a multilateral basis in order to reflect relevant countries' views. Therefore, it is inappropriate for the USG to set a unilateral standard and intervene in the setting of rates by imposing a condition on market entry (paragraph 75 - 90). Moreover, if a government thus intervenes and orders payments lower than the agreed-price on a commercial basis (paragraph 87 - 90), it will subsequently distort the commercial transactions.

3. Since the international settlement rate system strongly influences the basic structure of international telephone services, it has been developed at the ITU through

the consensus of its members. It is of course desirable that settlement rates should become more cost-based and be further reduced. However, the issue has already been discussed at international organizations such as the ITU and the Organization for Economic Cooperation and Development (OECD), and further discussion is required to achieve a system to which every member can agree.

4. The promotion of competition should achieve the lowering of international settlement rates. The FCC proposal, nevertheless, will hamper the promotion of competition because it makes carriers' entry into market for international services difficult. As a result, users will enjoy less benefits than they are supposed to from rate reductions and diversification of services.

5. With regard to international services, we would not deny the possibility of trade distortion caused by monopolist carriers bypassing the international settlement rate system in non-liberalized countries. However, safeguard measures against such possibility should be ex-post and be consistent with the GATS Principles.

6. In light of the above, the FCC proposal (paragraph 75 - 86) poses the following problems:

(1) According to the NPRM, it is a condition for authorization that the settlement rates stay within a benchmark range (paragraph 76 and 82). This is to impose a heavy burden on the carriers which wish to enter into the U.S. market, and is to make a practical barrier to their entry.

(2) International settlement rates are normally based on commercial contracts between carriers. Therefore, it is not appropriate to oblige the carriers to fulfill a certain level of such rates as a condition for their entry to the U.S. market. Such an obligation will also be quite unreasonable for carriers which do not provide

international telephone services on the route they intend to enter, because their market entry will have to be contingent upon the level of settlement rates over which they have no control.

(3) According to the NPRM, the FCC can order all U.S. carriers to reduce settlement rates to the bottom of the benchmark range if the FCC finds trade distortion on the route after a certain carrier has entered the U.S. market (paragraph 76 and 82). However, if such a distortion of trade occurs, measures should be taken only against the carrier itself, and it is by no means appropriate to order the foreign carriers, which have nothing to do with the distortion, to lower their settlement rates.

(4) Also, the FCC proposal stipulates that if settlement rates are beyond the benchmark range, no carrier will be allowed to provide an international private line resale service (paragraph 82). Such a measure would not only impede the promotion of competition to the detriment of users, but also constitute unnecessary restrictions.

7. Distortion of trade through the bypassing of the international settlement rate system is not likely to occur, and even if it could be the case, it would only be a temporary problem among liberalized countries because the U.S. carriers can take countermeasures on their side. Thus, excessive government intervention should rather be avoided amongst liberalized countries.

According to the NPRM, the level of settlement rates has been proposed as a condition on market entry for foreign affiliated carriers in order to prevent foreign carriers from distorting competition in the U.S. market by cross-subsidization between them and their U.S. affiliates through the use of above-cost settlement rates (paragraph 80). However, trade distortion created by bypassing settlement rates can be rectified by proportionate return obligations as an ex-post measure, and cross-subsidization can be avoided by less restrictive measures, such as proper application of regulations on users' rates. Therefore, the proposed measure proves to be unnecessarily burdensome.

The FCC, in principle, applies the same settlement rate for a route between the U.S. and all other countries. However, according to the NPRM, different benchmark rates are applied and U.S. settlement rates vary in accordance with country-group categorizations. This means that U.S. carriers charge other countries' carriers above-cost settlement rates depending on country groups. This is inconsistent with the principle that settlement rates should be cost-based.

8. According to the NPRM, the FCC sets a benchmark, and authorization for the U.S. market entry depends on the settlement rate level for each route (paragraph 75 - 86). However, if divergent standards and different transition periods are used based upon the classification of countries into three categories (upper income countries, middle income countries and lower income countries), it could constitute discrimination and thus be inconsistent with the MFN Principle of GATS Article 2. Also, the gap between the standard and the real cost, as well as the burden of meeting the benchmark, greatly differs for each country of the same group. This point also indicates that the FCC proposal could be inconsistent with the MFN Principle.

According to the NPRM, furthermore, carriers are authorized to provide facilities-based services only if their foreign affiliates (defined as "owning a greater than 25% interest in, or controls the U.S. carrier" (paragraph 76 and footnote 129)) offer a settlement rate within the benchmark range. This means that only foreign-related carriers are subject to the benchmark condition, and that the FCC proposal could also be inconsistent with the National Treatment Principle of GATS Article 17.

9. In contrast, the GOJ has made efforts to facilitate market entry into international services. In the WTO/GBT negotiations, the GOJ is offering to abrogate foreign ownership restrictions on the new market entry of type 1 facility-based carriers. The GOJ has also decided, as its own deregulatory initiative, to delete the provision in

the Telecommunications Business Law that is meant to prevent excess telecommunication facilities. With regard to type 2 resale-based carriers, 100% foreign participation has already been realized, and the procedure for registration is concluded within 15 days from the submission of an application. Many foreign carriers, including those from the U.S. such as AT&T, MCI and Sprint, have already entered the Japanese market. This rule will also apply to international simple resale services from 1998. In other words, after 1998, the Japanese market will become fully open to all carriers around the world in that the GOJ will no longer be able to prevent any foreign carriers, whether type 1 or type 2, from entering the market.

On the other hand, it will be unnecessarily restrictive if the entry of a Japanese carrier into the U.S. market is barred simply because the settlement rate between Japan and the U.S. is beyond the benchmark range set by the U.S.. The GOJ thus strongly requests that the U.S. rules be as open and transparent as those of Japan.

10. International services are one of the major issues at the WTO/GBT negotiations, the deadline of which is approaching. The measures taken to resolve this issue must be consistent with the GATS Principles. Nevertheless, it remains unclear whether the proposal in the NPRM is consistent with the GATS Principles, and we have a deep concern that it may have an adverse effect on the successful conclusion of the negotiations. We are particularly concerned that developing countries might be discouraged by the proposal.

11. We wish to receive clarifications on the following points regarding the NPRM, in preparation for submitting further comments, as necessary:

(1) It is mentioned that "in competitive markets our benchmark rates would not be necessary" (paragraph 69). In what specific situation are the benchmark rates not invoked?

How does the above situation relate to a country to which the flexibility order (CC. Docket (No. 90 – 337.) Phase II, adopted on November 26, 1996) applies? Given the understanding that the flexibility order is a means to promote liberalization of settlement rates, for what reason will the benchmark rates apply to the liberalized routes?

(2) With regard to routes on which the benchmark is not applied, is no restrictive measure described in the NPRM, including safeguards against distortion of competition, to be imposed? Since safeguards already exist in the flexibility order, no other restrictive measures seems to be necessary. How does the NPRM deal with this point?

(3) What specific situations are regarded as distortions of competition in the NPRM and in the flexibility order?

(4) It is suggested in the NPRM that the ECO test might be maintained after the proposal is brought into effect (paragraph 78 and 85). How and in what situation would any possibility or room remain for the ECO test to be maintained? It should be noted that, as the GOJ has repeatedly pointed out in the WTO/GBT negotiations, the GOJ believes the ECO test is inconsistent with the MFN Principle and should be abolished.

12. The GOJ strongly hopes that, in response to GOJ's comments, the USG will reconsider the proposal to ensure consistency with the GATS Principles and the promotion of competition, so that the WTO/GBT negotiations will be successfully concluded and that a framework will be created for the worldwide liberalization of telecommunications.